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Centrally Planned Economies in Europe

Economic Overview 1985

Dr. Josef Adamek

A Research Report from The Conference Board

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Preface

The present Report constitutes an attempt to highlight, as objectively and dispassionately as possible, changing patterns in Europe's centrally planned economies. As such, it eschews value judgments on centrally planned economic systems *per se* and keeps to a minimum comment on the political bias they reflect. This Report differs from its predecessors in 1983 and 1984 to the extent that it focuses exclusively on centrally planned economies in Europe: the Soviet Union, the European COMECON member states, and Yugoslavia. In each instance, an effort is made to identify significant trends in the economy as a whole and to examine in some detail changing patterns in foreign trade, with particular emphasis on trade with the West.

The annual Conference Board *Overview of Centrally Planned Economies* has come to be regarded as a valuable source of objective, clearly presented information. I am confident that this Report carries on that tradition.

October 1985

JAMES T. MILLS
President
The Conference Board

COMECON: New Emphasis on Integration

The Summit of the Council for Mutual Economic Assistance (COMECON) announced by Leonid Brezhnev in 1981 finally took place on June 12-14, 1984. Senior party officials and government leaders from the ten COMECON member states (non-European members Cuba, Mongolia and Vietnam were also represented) acknowledged the shortcomings of the so-called "Complex Program" of economic integration agreed in 1971 and adopted a new policy document designed to accelerate and streamline economic integration within the alliance.

The new longer-term strategy identified four key objectives:
- Closer coordination of COMECON member states' economic and policy planning generally;
- Joint fifteen to twenty-year technical and scientific programs in vital sectors (identified as *inter alia* automation, electronics, atomic energy and space technology);
- Direct (*i.e.*, cross-frontier) cooperation between individual industrial enterprises in COMECON and, where appropriate and feasible, the establishment of "multilateral" industrial firms; and
- Joint solutions to major problems of mutual concern.

The "new" strategy is reminiscent of many similar pronouncements since Stalin's death and is couched in language so vague as to preclude detailed commentary. Nonetheless, certain observations seem to be admissible.

Points one and two - "closer coordination" and "joint programs" - are self-evident to the extent that they are implicit in the decision to set up COMECON in the first place; further, the target sectors enumerated are predictable and, as such, offer no new insights.

By contrast, points three and four highlight the fact that COMECON member states have been and are put under deliberate pressure to orient their economic strategies inwards, *i.e.*, towards Moscow.

Even under the tough Andropov regime, however, the German Democratic Republic, Hungary and Romania made no secret of the economic impracticality of such a move: not only did they have serious debt repayment obligations which had to be serviced in hard currency, they also showed increasing signs of "enjoying" trade with the West and increasing acceptance of and reliance on imported Western goods and technology.

Early in 1984, Hungary went on record that it felt entitled as a socialist state within the Soviet alliance to take such steps as appeared necessary to determine and defend its own economic interests. When Hungary was rebuked by the staunchly pro-Soviet Czechoslovak Government for attempting to maintain an "intolerable level of involvement" with the West, the East Germans firmly stated their understanding of and support for the Hungarian position. A further much-publicized gesture of support came in the form of a state visit by East German leader Erich Honecker to Romania, immediately after the latter had reaffirmed its commitment to keeping open the trade door to the West.

It should be stressed that these were more than token gestures. Within the overall confines of East Bloc politics, they must be seen as pragmatism at its most courageous.

The tension eased somewhat when Andropov fell ill. After his death and the advent of Chernenko, no unanimity was descernible; no clear directives were issued. Seasoned observers of the East Bloc

scene reported a sense of disunity, of drift, of disillusionment with the transitional nature of Soviet leadership. The time was ripe for some of Europe's centrally planned economies to stake a claim for additional autonomy and, with the clear exception of Czechoslovakia, they acted accordingly; to what effect emerges from the individual country analyses *infra*.

The relationship between COMECON and the European Community has been, to say the least, strained; no formal contact has existed since 1981. It is significant that the overtures made with a view to putting things on a more formal footing again came not from Brussels but from Moscow. A letter was addressed to the President of the European Commission on June 14, 1985 proposing that the two organizations issue a joint statement as to their relationship and future cooperation. The European Community response was cool: the letter was acknowledged but no firm undertakings were announced.

COMECON courtship of the Community is understandable: well over a third of COMECON trade with countries outside the COMECON alliance is with the Community. In 1984, COMECON/European Community trade balance figures published by the European Commission showed a US $ 10 billion* surplus in favor of the former, due primarily to COMECON exports of natural gas and raw materials; by contrast, the European Community derives less than 10% of its third-country trade revenue from COMECON sources.

For two-way trade between the two groups to take off, COMECON will have to develop some incentives to match European Community tariff and quota concessions.

* Throughout this *Overview*, the term "billion" refers to 1,000 million, *i.e.*, 1,000,000,000.

THE SOVIET UNION: The Winds of Change?

Prognoses and Performance

Over the course of the last two decades there has been one remarkably consistent feature of the Soviet economy, namely the almost monotonous regularity with which successive Five-Year Plans have proved to be incapable of full realization. 1985 is the final year of the current Plan and it is already conceded that 1981-85 targets will not be reached.

The Plan for 1985 envisages growth of net material product by 3.5%, a 3.9% increase in industrial output, 6.7% growth in agriculture, 3.3% growth in transport, and 3.4% in investment. Not only are these targets optimistic (the International Monetary Fund predicts across-the-board economic growth for 1985 of between 2.5 and 3%), they are also such that, even if they were to be reached, overall targets for the Five-Year Plan 1981-85 can now no longer be attained.

It is instructive to review 1984 performance in the light of targets set for the current year. Official figures* published in *Izvestiya* claim that net material product** grew by 2.6% in 1984, seasonally adjusted to 2.2%. Gross agricultural product declined in 1984 (−0.3%), crude oil production shaded for the first time since World War Two; coal production has been stagnant since 1978; and new investment fell significantly short of the 3.9% postulated.

Armament production and research continued to be regarded as top priority. These efforts concentrated on the research and development of ICBMs, giant aircraft carriers, cruisers, strategic bombers, submarines, star war technology, lasers, biological weapons and other new warfare technology.

Assessment of these efforts differed widely in the West. In February 1985, the CIA and the Pentagon issued a joint statement which concluded that Soviet military spending exceeded that of the United States "by substantial margins" despite the slowdown in the Soviet economy.

The mortality rate - the economic significance of which need not be stressed - rose by 47% in the period 1960-80 (according to *Izvestiya*) and increased from 7.1 per thousand to 10.4 per thousand. There was a record decrease in life expectancy from 67 to 62 years in the period 1964-80, particularly in males and new-born infants; this decrease is mainly attribuable to deteriorating health care, widespread and increasing alcoholism, traffic accidents and accidents at the workplace.

There were, however, some bright spots.

Industrial output grew by some 3.9% in the course of 1984, according to official Government figures, thereby exceeding the 3.4% set out in the 1984 Plan. Moreover, in some industrial sectors, growth was firm, not to say impressive: the chemical industry boosted output by some 5%; mechanical engineering showed 7% growth (triggered in part by

* In the absence of a specific statement to the contrary, the figures cited in this Report are those released by individual ministries or state agencies in the specific jurisdiction under review. Whether or not they are *accurate* is, ultimately, of less consequence than the fact that, on the whole, they are plotted consistently from one year to the next, implying that reasonably *accurate comparisons* can be made and specific trends extrapolated. The present Overview adopts this approach.

** Countries with centrally planned economies do not use the two most familiar measures of national output, namely gross domestic product (GDP) and gross national product (GNP); instead, aggregated national income is habitually referred to as "net material product" (NMP), a term which connotes material output and services deemed "productive", *i.e.*, as adding to the overall "wealth" of the economy.

machine tools, up 28%, and industrial handling equipment, up 25%); and natural gas production rose by 9.6% to offset declining output of oil and coal.

As in many other countries (and by no means exclusively those with centrally planned economies), a tabulation of procentual increases and decreases by individual market sector can obscure rather than illuminate the overall economic picture. As far as the Soviet Union is concerned, this obscurity is compounded to the extent that annual statistics are "adjusted" for cosmetic and substantive political reasons; in a really poor year for a given market sector there have been occasions when the decision was taken to issue no figures whatsoever.

Nowhere is this better documented than in the area of military expenditures. At a session of the Supreme Soviet in November 1984, it was announced that the military budget was being increased "by 12%". This is a demonstrably fictive figure, since it does not take into account military R & D, stockpiling of weaponry, civil defense, paramilitary operations and clandestine activities. All of these outlays are, of course, concealed under non-military headings.

Accordingly, the most revealing set of statistics in terms of the overall economic performance of the Soviet Union over the last two decades are those which chart procentual year-on-year growth in industry and agriculture. These figures - which were officially released in *Izvestiya* - exhibit an inexorable downward trend:

Soviet Industry and Agriculture: % Growth 1966-84

Period	Industry	Agriculture
1966-70	8.5	3.9
1971-75	7.4	2.4
1976-80	4.4	1.7
1981-84	3.6	0.7

Expressed as % of gross output.

Problems, Remedies, Potential

The figures in the above table leave no room for doubt that the Soviet Union has problems. There is evidence, however, that the search for remedies is being intensified. Above all, it must never be forgotten that the Soviet Union is and will remain a superpower, not only in terms of military might but also in terms of economic potential (see box).

The USSR: resources and potential

Currently, the Soviet Union is the world's leading source or producer of asbestos, cement, chromium, iron, manganese, mercury, natural gas, nickel, petroleum (cf. infra), *platinum, steel, tin and titanium. It is in number two position for aluminum, gold, magnesium, phosphate rock and tungsten, and in third position as regards antimony, copper, molybdenum and silver.*

It is also worth recalling that the Soviet Union is the world's third-largest coal producer; that it is the second-largest electricity producer; that it has the world's greatest hydroelectric resources; that the largest nuclear reactor commissioned in the world to date, the 1,500-MW Ignalinsk-I unit, reached full power in 1984, with a second unit now under construction and two more scheduled for the 1990s; that it is a leader in ultra-high voltage electricity transmission (with 1,500 km of line network scheduled to be operational before the end of the century); and that Soviet petroleum output (12,520,000 bbl/day) overtook that of the Middle East as a whole (12,005,000 bbl/day) in 1983.

The full extent of the Soviet Union's massive reserves of gold, diamonds and other precious metals has never been convincingly assessed.

Tapping all this potential has, of course, always proved extremely difficult. Severe problems persist not only in extraction (some 85% of the Soviet Union's recoverable "published proved" mineral deposits lie in the permafrost wastes of Siberia), but also in terms of refining and onward processing, transportation and distribution, not to mention efficient coordination of these different operational phases.

A change in attitude is the first prerequisite if this potential is to be exploited. Whether or not centrally planned economies are all intrinsically slow, ponderous and inefficient is not at issue here; what *is* at issue is whether specific responses can be formulated to specific problems. In this context, two - at first sight, banal - pronouncements seem worthy of mention:

- In June 1984, the official government organ *Izvestiya* featured a critique of Soviet industry and expatiated on the barriers to efficiency and innovation. It was argued that, as yet, no effective economic mechanism existed in the Soviet Union to regulate the relationship between science and production; until such a mechanism was in place, no changes in the rates of development of scientific-technical progress could be anticipated.

- The Economic Institute of the Novosibirsk Academy of Sciences prepared a confidential report on the Soviet economy which stated that the Soviet Union was "no longer" *(sic)* able to secure the efficient use of its resources; a centralized bureaucracy directing the economy acts as a brake by maintaining the *status quo* and condemning the country to living in a model devised by Stalin 30 years ago which is unadapted and unadaptable to the needs of a modern economy.

Official dissatisfaction with dogmatic models prompted the Economic Experiment launched at the beginning of 1984. The first phase saw increased independence for some 2,300 enterprises representing some 12% of total industrial production; a second phase, initiated at the beginning of 1985, bears some of the hallmarks of a market economy, notably as regards a waiver of rigid production quota controls and a new flexibility as regards pricing policies. (This experiment and extensions to it are reviewed in more detail at *Economic Highlights and Action Programs* below.)

It is arguable, however, that the advent to power of Mikhail Gorbachev in the spring of 1985 will herald dramatic and far-reaching changes in Soviet economic policy. By conventional Soviet consensus government standards, the new Kremlin supremo shows no small measure of ruthlessness: ten ministers have been axed, as have twenty regional party secretaries; four new faces are seen in the Politburo; a new foreign minister has been appointed; the original Five-Year Plan for 1986-90 has been revised out of all recognition; and sweeping social and consumer reforms have been introduced (the most publicised of which undoubtedly were the curbs imposed on vodka consumption).

The consensus among Kremlinologists, however, is that the new-style leadership will not affect the political system *per se*; nothing in Mr. Gorbachev's background suggests that he will dilute in any way the Communist Party's monopoly of power or the Soviet Union's traditional stranglehold on COMECON.

What he *is* expected to do - and what he has in some measure already done - is to devolve economic powers and responsibilities away from the centre towards the regions; to place new emphasis on personal responsibility *and* accountability at all levels from shopfloor to ministry; and to promote the concept of "quality" and profitability at regional and local levels.

The West often views the Soviet Union simply as "Russia" but it must be recalled that the Union of the Soviet Socialist Republics is a federal state extending from eastern Europe through to northern Asia. And it is on Asia and Siberia that the Soviet Union will rely to stimulate economic recovery: in Azerbaidjan, Armenia, Kirgizia, Tadzhikistan, Turkmenistan and Uzbekistan. It is no coincidence that demographic trends pinpoint as the high population growth area of the Soviet Union that area to the immediate south of Siberia, a region which houses the Soviet Union's natural resources but one which has in the past been plagued by chronic labor shortages. The signs point to Gorbachev and his colleagues taking a wider view: sluggish economic development in European Russia is to be compensated by rapid progress in Asia.

Economic Highlights and Action Programs

It is clear that the comparatively youthful Mr. Gorbachev will make vigorous changes: with medical good fortune, however, he can look forward to fifteen or twenty years at the helm.

Accordingly, he is in no hurry to show his hand; his first priority is to capture the Soviet public's imagination (which he has done in his televised walkabouts).

Gorbachev's speech to the Central Committee at the end of April 1985 also suggested that he will tread warily: he deferred to the remaining members of the "old guard" from the Brezhnev days, stressing that he wanted to ensure the "proper blend of experience and youth". That speech provided precious little hard information on how he and his friends intend to right the economy. In essence, he was content to identify current weaknesses - poor management, worker apathy, low productivity, waste, reluctance to use new technology, and the age-old propensity for passing the rouble. In short, he demanded discipline and order - *poryadok* - rather than genuine reform.

The catalogue of true reforms may not be issued until February 1986 at the Party Congress which will endorse the next Five-Year Plan. Mr. Gorbachev has said, however, that 1986-90 must see an annual average rate of industrial growth in the order of 5.5%. (For the first six months of 1985, industrial growth was rising at a rate of only 2% projected on an annual basis.)

Perhaps the biggest question mark of all hangs over the Soviet Union's military policy. A deal with China to reduce military presence along the common border plus agreement in Geneva on missile reduction would liberate vast sums for injection into the Soviet economy.

Agriculture

For the sixth successive year, no data was published on grain crops. Bad weather, poor distribu-

tion and obsolescent equipment combined to yield disastrous results. Western specialists estimated the harvest at some 170 million tonnes, implying imports of between 45 and 50 million tonnes in 1984-85 to meet demand.

An action program was agreed in October 1984 to increase the total amount of irrigated and drained land by some 12 million hectares (almost 30 million acres) in the period 1985 through 2000. An estimated US $ 130 billion has been spent on irrigation and drainage over the past two decades. Conclusion: that available technology is inadequate and/or available knowhow deficient.

The perennial problem of bringing food to Russia's cities showed little signs of being alleviated.

Underproduction and transit wastage in 1984 saw appreciable decreases in margarine, vegetable oil and citrus fruit production. Cotton fell by 6.5%, sunflower seed by 10%. Increases were claimed for sugar beet, potato and vegetable crops.

Huge imports of grain and other agricultural products are again predicted for 1985-86.

According to the Soviet economics journal *Voprosy Ekonomiki* in January 1985, the USSR now hosts eight million "private" farmers; the ideology of Stalinist farm collectivization has atrophied as a result of the basic need for more (and better quality) food, particularly meat and dairy produce. The "private" farmers' plots are worked rather than owned privately; according to *Voprosy Ekonomiki,* the trend (the number of such private ventures has doubled in the last few years) does not constitute a political threat to the system. It concedes, however, that, despite regulation of livestock numbers and animal fodder allocations, these farms have flourished because they are more productive than state farms. These small (1 1/2-acre) plots add up to less than 5% of total farmland in the Soviet Union but deliver more than 25% of the country's agricultural produce by value: they account for more than two-thirds of the total potato crop and one-third of eggs, milk, meat and vegetables; 20% of the country's sheep, pigs and cattle graze on these farms.

Consumer Policy and Product Quality

Consumer protection as understood in Western market economies continues to figure well down the scale of Soviet priorities. This said, the Soviet consumer does stand to benefit from the new leadership's repeated insistence that product quality must be enhanced. Speaking at a Science and Technology Conference on June 11, 1985, Mr. Gorbachev lashed out at the general shoddiness of Soviet goods, noting that what passes for "top quality" in the Soviet Union would be labelled "substandard" elsewhere. Plant must be modernized and automated; waste and defects must be sharply reduced; and worker apathy must be counteracted.

Long-established reputations suffered and heads rolled. The minister for agricultural machinery and the minister for building materials had both opted for "easy targets" under successive Plans; the minister for the petrochemical industry had been profligate with imported equipment; and the minister for the steel industry had consistently failed to meet his Plan target because of "bad management".

Remedies outlined in the June 11 speech include a pruning of "middle management", *i.e.,* the middle level of the Soviet hierarchy, and according greater powers to sectoral planning bodies at one end of the scale and individual enterprises at the other.

To ensure that manufacture of substandard goods is penalized, Gorbachev argues that the pricing system must be restructured and wage patterns related to performance. He explained how in a front-page leader in *Pravda* on August 4, 1985:

- The "Andropov" experiment in mildly decentralized management (see page 11, *supra*) will be extended to all of Soviet industry by January 1, 1987;
- With effect from 1986, factories which produce goods ascertained to be below "top quality" will be subject to a 5% price penalty levied mainly on the fund earmarked for worker bonus programs; where no improvement is identified, further fines will be levied progressively; ultimately, the plant will be closed;
- By the same token, workers in factories earning "top quality" seal of approval will be awarded bonuses equivalent to up to 30% of the product manufacturing price; and
- Plant managers will be accorded wider powers to decide on re-tooling and modernization; in practice, they will be allowed to spend up to four million roubles without requesting specific approval from central government. Additionally, and with effect from 1987, such re-tooling and modernization subcontracts will be awarded locally rather than via Moscow. (This last proposal presumes that the Central Plan will be better implemented to ensure that raw materials and machinery are duly allocated to the regions.)

To date, there has been no criticism of these proposals in the Soviet Union. Western commentators point out, however, that they are not as sweeping as Mr. Gorbachev gave reason to anticipate; what is more, they rely on so-called "commissions of certification" and the decisions of inspectors rather than on consumer recognition of quality.

Social Programs

The Soviet Union Academy of Sciences stated recently that alcoholism could bring the country (literally) to its knees in 12 to 15 years if the current trend continues. Vodka kills one million people a year, there are an estimated 40 million alcoholics, and the demon alcohol is blamed for birth defects and contributing to an astonishing drop in adult male life expectancy from 67 to 62 years in the period 1964-80.

One suspects it was the serious economic effects of alcohol, however, which prompted the Soviet authorities to take action in May 1985: harsh penalties were introduced for drunken driving, a clampdown was announced on *samogon* (home brew) and reductions (but no rationing) in vodka production were announced for January 1986. The legal drinking age was raised from 18 to 21 years and opening times were curtailed by three hours.

If the Government has done its sums right, the annual loss in revenue from alcohol sales (some 45 billion roubles or some 10% of total income) will be offset by savings totalling some 200 billion roubles on absenteeism, low productivity, workplace accidents, and medical treatment. Soft drink production is being stepped up and keep-fit and recreation programs and facilities are to be extended.

Mr. Gorbachev's reorganization of the Politburo and regional party hierarchies is paralleled in a zealous drive to eliminate corruption, embezzlement, data falsification and outright incompetence and shirking.

The clean-up campaign and the prosecutions under it have received wide coverage in the Soviet media. An accountant from Kiev was executed by firing squad for cooking the books; an ex-Minister of the Interior was termed corrupt, stripped of his general's rank and the privileges attaching to it, and subsequently found dead, allegedly by suicide; and *Pravda* inveighed against cover-ups in high places following an orgy arranged by a police chief in Kursk.

Clearly, the aim is to demonstrate openness in government on the one hand and mitigate revenue losses via the black economy on the other.

Transportation

Among the Soviet Union's infrastructure problems, transportation is perhaps the most serious. Chaotic distribution of agricultural and industrial products is endemic: *Izvestiya* reported that, at any one time last year, no less than one third of the country's road transport vehicles were out of commission. Since some 85% of the country's needs have to be brought in to European Russia from the east, some solution must be found. The situation is reported to have improved somewhat since the new Baikal-Amur railway link was completed in October 1984.

COMECON Trade

The pattern of Soviet trade with fellow COMECON member states can be discerned from the following table based on official USSR foreign trade statistics. Results are shown for the years 1981 through 1983, the most recent year for which full statistics for each jurisdiction are currently (September 1985) available:

Trade with European COMECON countries saw a higher increase in exports (up 11.1%) than imports (up 10.7%). As noted in the introduction to this section, the Soviet Union made an effort to stimulate exports from various COMECON countries inwards towards the USSR.

The major stumbling block in the past has been that Soviet Union exports to these countries (predomi-

SOVIET TRADE WITH EUROPEAN COMECON COUNTRIES
(Total in 000,000 roubles at current prices)

	Exports			Imports		
Country	1981	1982	1983	1981	1982	1983
Bulgaria	4,374.5	4,884.6	5,510.8	3,696.9	4,288.1	5,053.3
Czechoslovakia	4,382.3	5,047.5	5,871.6	4,104.8	4,731.9	5,420.4
East Germany	5.526.1	6,419.6	6,797.8	5,154.6	5,776.2	6,595.7
Hungary	3,306.7	3,707.2	4,058.0	3,300.4	3,746.4	4,007.0
Poland	4,931.3	4,812.9	5,274.3	3,220.8	4,097.0	4,786.7
Romania	1,779.1	1,423.6	1,639.6	1,673.1	1,683.4	1,665.3

Source: Foreign Trade Statistics, Moscow.

nantly fuels, energy and raw materials) were paid in industrial equipment and goods which were generally second-rate: the better-quality goods were reserved in many instances for export to the West to earn the hard currency needed to service outstanding European COMECON member country debt and to secure credits for further imports of Western goods and technology.

In an attempt to resolve this dilemma and ensure its access to better-quality technology and product, the Soviet Union has, on the one hand, made proposals for extensive exchanges of knowhow between industrial enterprises within COMECON and, on the other, has concluded longer-term Economic and Scientific Cooperation Programs with individual countries which lay down specific requirements in respect of investments to be made by them and minimum quality requirements in respect of their exports to the Soviet Union. The major export categories are foodstuffs, industrial consumer goods, plant and equipment.

Education: The Age of the Computer

A significant longer-term change was introduced in September 1984 when the admission age to first grade was reduced from seven to six years. This implies an additional 1.2 million children in school in 1984-85, rising to some 4 million by the beginning of the next decade.

Deliberate emphasis is laid on upgrading educational facilities generally. In 1985, some 200 Soviet schools and 300 training units started using personal computers; according to *Izvestiya,* substantial increase in personal computer use is predicted following redefined COCOM (Coordinating Committee for Multilateral Export Controls) rules effective July 1984 with regard to software and telecommunications generally. Models made in Eastern Europe and the Soviet Union tend to be based on Western computer technology of a decade and a half ago, however, and, although COMECON cooperation has yielded the Ryad computer system, member countries' hardware is frequently incompatible. In practice, the Soviet Union relies heavily on East German computer technology, by far the most sophisticated in the East Bloc (albeit virtually indistinguishable from IBM 360 mainframes).

Energy

The Soviet Union ranks third in coal production worldwide and leads the field in petroleum and natural gas. In the longer term this will undoubtedly prove to be of benefit; a comparative surfeit of energy in Europe at present has forced down prices and export revenues in the main Soviet markets. The Soviet Union pipes natural gas to Austria, France, Italy, Turkey and West Germany and, on July 14, 1984, announced new supply pipelines to service its COMECON neighbors.

Despite the comparative energy glut worldwide, the Soviet Union is laying emphasis on energy conservation and recuperation. The floundering steel sector is to be revitalized with the progressive elimination of open-hearth casting and the introduction of continuous casting technology. In this sector in particular, a significant market is developing for turnkey plant featuring energy recovery and secondary use technology.

The 613 million tonnes of oil produced last year (1984) showed a drop of some 3 to 4 million tonnes over the preceding year; the first half of 1985 has seen production fall by around 4% and the 1985 target (628 million tonnes) is unlikely to be met. The underperforming oil industry is also hit by falling world oil prices which deplete the country's hard-currency earning potential (US $ 19 billion in 1984, *i.e.,* around two-thirds of the Soviet Union's hard-currency income). It is something of a paradox that the strength of the dollar has softened the blow: the USSR pays for its imports from Western Europe in hard currency with the result that, although the dollar price for Soviet crude dropped in 1984, the purchasing power revenue it generated showed an increase of some 12% when translated into, say, pounds sterling.

A plan has been outlined to increase deep oil drilling by 40% over the next five years to arrest the decline in oil production.

Industry and Labor

Salient aspects of the Soviet Union's plans for industrial reform have been alluded to in preceding sections. In essence, the revitalization of Soviet industry implies:

- Better utilization of energy resources and improved energy conservation;
- Radical updating of industrial plant and equipment with an emphasis on automation, robotics, high-tech components and computer-assisted production;
- Stringent new quality controls;
- Devolution of purchasing power and decision-making to regional/local centers;
- Introduction of penalty and incentive programs to raise product quality; and
- A possible widening of pay differentials.

The last point requires some elucidation. Experience in the West has generally shown that wider

differentials are effective only when the workforce is well-trained and hardworking. As a rule, the average Soviet worker is neither. Moreover, although wages are low by Western standards, an employee's monthly overheads (housing, transport, electricity) have to be heavily subsidised, the result being that - procentually at least - the average worker's "spending money" is actually higher than in most Western countries. Further, luxury items are either unavailable or priced out of his range or so limited in choice that "extra" spending money represents no great attraction. It is principally for this reason that personal savings are comparatively high in the Soviet Union. It seems feasible that the penalty/incentive program outlined by Mr. Gorbachev will only begin to bite when the range of consumer goods is widened.

Given that the immediate prospects for Soviet agriculture are none too bright, the 5.5% growth predicted in the next Five-Year Plan will *de facto* be industry-led. Consequently, the Soviet leadership will be anxious to see a rallying of oil and gas prices in as short a time frame as possible.

Implications for Trade with the West

It goes without saying that the Soviet Union is anxious to acquire foreign technology. It appears that several gateways are exploited:
- Piracy of technical data and equipment, often via dummy corporations set up abroad, the net result being that much Soviet equipment is a reasonable facsimile if not an exact duplicate of, say, U.S. or West German products;
- The "side-door" approach utilizing those countries which have regular and reasonably unlimited access to foreign high technology (Hungary, East Germany, Romania); and
- "Legitimate", *i.e.,* direct access to the market.

It is to be hoped that the opportunities which currently exist for foreign exports to the Soviet Union are evidenced both explicity and implicitly in the preceding pages. In short, key areas of export potential relate to:

- metallurgical plant and processing technology
- turnkey plant in the chemical, petrochemical and plastics industries
- gas and oil extractive plant and equipment
- irrigation and drainage plant and knowhow
- large diameter pipes
- compressor equipment
- food processing and packaging plant
- automotive vehicle plant and technology
- wood treatment plants and paper mills
- robotics
- on-line product control and monitoring systems
- computer hardware and software
- metal finishing and surface treatment technology
- energy recuperation plant and knowhow
- soft drinks
- sport and recreation articles.

At present, the Soviet Union has a trade surplus with the West (see *Financial Position and Investment Intentions,* infra) and thus has some cash in hand, not forgetting a quite substantial amount of hard currency out on loan to Third World countries.

At the start of 1985, the Soviet Union demonstrated that it was not afraid to shop around in the West by ordering a US $ 450 million steel cord plant from Austria's Voest-Alpine Group and a $ 100 million shoe factory installation from Cogolo of Italy. Indeed, as this *Overview* went to press, it was confirmed that Sidmar, the Belgian steel group controlled by Arbed of Luxembourg, had agreed a 75 billion BF five-year deal with the Soviet Union for five million tonnes of specially treated steel sheet for use in the Soviet automotive industry.

It is inconceivable that major opportunities of this kind should not open up for Western suppliers once the proposed new Siberian gas pipeline to Eastern Europe starts construction. Further, plant and equipment will be required for factory units and development zones along the 3,145 km Baikal-Amur railroad, and for proposed expansion of the chemical and plastics sectors.

It has been mooted that, within the framework of the next Five-Year Plan, the Soviet Union would "prefer" to deal with Western Europe and Japan rather than with the United States. This attitude is said to be in response to U.S. sanctions on grain and U.S. efforts to persuade (as it happened, in vain) European and Japanese companies not to honor their trans-Siberian pipeline contractual commitments. If the Soviet Union does follow this route, however, the economic consequences for the United States will scarcely be felt. It should be recalled that total Soviet imports from OECD countries in 1984 came to no more than 2% of total OECD exports. As far as the United States is concerned, its exports to the Soviet Union are almost exclusively of the grains and cereals variety: the Soviet Union is not likely to prejudice a potential source of food supply in the interests of scoring an ideological debating point.

A new development in this context is that Western suppliers are being asked to accept a 10%-of-contract-price penalty in the event that their national governments subsequently embargo a signed contract or a part thereof. To date, no instance has been reported of such a penalty being enforced.

Financial Position and Investment Intentions

According to *Izvestiya,* Soviet foreign trade in 1984 saw equal total growth of both exports and imports by 9.6%. Growth of trade with the industrial West was slower, however, with exports increasing by 8.1% and imports rising by 4.8%. This resulted in a surplus in the Soviet Union's favor of US $ 2.1 billion.

The surplus with developing countries decreased from US $ 4.5 to 4.3 billion. It is alleged in the West that a large part of OPEC oil shipments to the USSR relate to payments for arms; thus, some $ 300 million in oil sales from Saudi Arabia is seen as payment on behalf of Iraq in respect of Soviet military assistance.

Clearly, these transactions are not reflected in official Soviet export statistics.

Trade within COMECON and with the West was reviewed in greater detail *supra*.

The Soviet Union raised considerable (± US $ 1 billion) funds in foreign markets in 1984, generally in the form of syndicated loans from Western European, Japanese and Middle Eastern banks. At the same time, the Soviet Union itself extended convertible currency credits to developing countries.

For 1985 as a whole, the external position of the Soviet Union should weaken, particularly because of fresh imports of grain, tapering energy receipts and increased domestic consumption. The impact could certainly be cushioned by increased sales of non-monetary gold.

Overall, investment is projected to rise by 3.4% in 1985. The 1984 target (3.9%) was not attained.

POLAND: The Doldrums of Indebtedness

On May 4, 1984, Polish Premier General Wojciech Jaruzelski signed a 15-year economic, technical and scientific cooperation agreement between Poland and the Soviet Union designed to reduce Polish dependence on the West and reinstate Poland as one of the strong trading partners of the Soviet Union within the COMECON alliance.

Poland's unequivocal commitment to COMECON showed scant regard for certain economic realities. Above all, it omitted reference to Poland's massive foreign indebtedness, the central problem to be resolved before any genuine economic recovery can be anticipated.

The Reagan Administration withdrew its opposition to Poland's acceptance in the International Monetary Fund in December 1984 and there are strong indications that Poland will be admitted in 1986.

In real terms, what this means is access to hard-currency top-up funding in the form of direct IMF loans and a degree of respectability in the eyes of potential new lenders. What it also means, however, is that the Jaruzelski regime will have to abide by IMF rules, not least in terms of better economic management. This, in turn, translates as even harsher austerity measures at home.

A first priority when the IMF team visited Warsaw in February 1985 was to establish how Poland's US$27.4 billion total debt could effectively be re-scheduled. The hiatus which followed martial law meant that more than $11 billion of unpaid principal and interest had accumulated since 1982, an amount several times greater than Poland's current annual hard-currency earning capacity.

In mid-July, a re-scheduling program was agreed: Poland was granted eleven years (*i.e.*, to 1995) to repay the $11 billion outstanding in favor of the 17 members of the Paris Club; additionally, a five-year grace period will apply.

Results and Prognoses 1984-86

First signs of economic growth detected in 1983 continued into 1984. Last year, net material product increased by 5%, with increased volume of production in industry, agriculture and construction. Gross industrial output increased in 1984 by 5.3%: coal, natural gas, synthetics and radios showed increases; coke, sea-going vessel construction, fertilizers, detergents, sulfur, sugar and meat production declined; petrochemicals stagnated. Gross agricultural output increased by 5.7%, with crops up 7.6% and livestock levels up 3.4%. Excellent weather conditions boosted grain output to a record level of 24.4 million tonnes. Construction increased by 6.9% following a growth in investment of some 12%.

The Plan for 1985 pegged growth of net material product at 3.7%. Investment was not scheduled to increase. Agricultural production will decline, but industrial output is to grow by between 4 and 4.5%. The 1985 Plan is modest in its expectations but, even if the 1985 Plan is fulfilled, the original targets set out in the *Stabilization Program 1983-1985* will not be met.

Supplies to the consumer market in 1985 will be some 10% lower than in 1979 and the total volume of investment and of income from the West lower by some 40%.

Foreign trade trends and expectations are reviewed separately under *Prospects For Foreign Trade* below.

Will the comparatively modest expectations set out in the 1985 Plan be fulfilled? Current analysis suggests they will not. A hard winter in 1984-85 meant that the year started slowly. Agriculture, mining and industry generally were affected. Exports showed no significant expansion. The persistent decrease in Polish hard-currency export earnings in the first half of 1985, coupled with increased imports, reduced the country's hard currency surplus; Poland's trade deficit with the rouble zone increased concurrently.

A draft plan for 1986 was submitted in June 1985 and will be ratified before the end of this year. Industrial output is to increase by 3.2 to 3.5%, with the strongest emphasis on engineering (+5%), chemicals (+4.1%) and light industry (2.1%); metallurgy is projected to improve by a slimmer margin (+1.5%). An increase of 6% is anticipated in investment, with the main stress on infrastructure modernization and rebuilding. No significant change is expected as regards trade with the West.

ECONOMIC DEVELOPMENT UP TO 1990: THE LODZ INSTITUTE FORECAST

The Econometric and Statistics Institute in Lodz predicted in a May 1985 *Forecast* that NMP levels originally attained in 1978 will not be matched again until 1988, assuming however that:

- a trade *surplus* with the West can be maintained,
- a trade *deficit* with COMECON countries can be maintained;
- investment will grow by 7% annually; and
- the present wage freeze can be continued.

On these assumptions, the following leading indicator predictions are made:

Indicator	Increase 1990/85
Net material product	20.5
Total production	22.6
Industry	26.0
Investment, *of which*	35.3
consumer durables	12.6
industrial	36.5
Employment	2.0
Imports	34.6
of which from West	37.3
Cost of living index	30.2
Real disposable incomes	12.1

Prices, Wages, Living Standards

Standards of living have fallen rapidly and, even on the best estimates, Poles can expect to regain pre-crisis levels of comparative prosperity by 1988-90 at the earliest. For 1984 as a whole, nominal wages grew by 20.2%, but consumer price increases of some 18% kept growth of real disposable incomes to a minimum.

Price hikes announced at the beginning of 1985 saw 12-13% increases in overall food, rent and energy prices.

Longer-Term Programs

In Spring 1985, the government announced a new *Five-Year Modernization Program for the Food-Processing Industry* designed in the first instance to combat domestic shortages and, subsequently, to promote expansion of agricultural produce and food product exports. The plan has an overall budget totalling US$5.8 billion over the period 1985-1989, with some 20% of this earmarked for hard-currency imports of machinery and equipment from the West. Key areas of development are:

- completion and modernization of dairy complexes
- construction and enlargement of grain mill storage capacities
- modernization and development of bakeries
- vegetable oil processing
- fruit and vegetable processing
- building of new and modernization of existing sugar refineries
- expansion of the tobacco industry
- expansion and building of new warehouses; and
- expansion of the food packaging industry.

In March, prices of ten essential foods were raised by between 30 and 75% (at the same time, an undertaking was given to de-ration grain products and raise pension levels); in April, fuel and electricity prices rose by between 20 and 32%; since June, butter prices are up to 22% higher and edible fats up to 82% higher; since July, meat, pork and poultry prices have increased by some 15%.

In the mid-seventies, the typical Polish family had to wait anything between eight and twelve years to be allocated low-cost housing; by 1984, the waiting period had increased to somewhere between sixteen and twenty years.

Government reform plans, which focus on raising prices and widening pay differentials, are resented inasmuch as they tend to discriminate against the "ordinary" worker; the government has moved

shrewdly, however, to ensure that employees in major industrial plants and in the mining industry (*i.e.*, those who comprised the backbone of Solidarity) have been accorded wage increases and fringe benefits roughly in line with price rises.

Prospects For Foreign Trade

Assessment of Poland's foreign trade position is complicated by progressive zloty devaluation against both rouble and dollar. For 1984, devaluation against the rouble averaged 4.9%, devaluation against the dollar 24.1%. Further devaluations in January (12.1%) and June 1985 (16.8%) mean that the zloty now stands at +/− 159 to the dollar and 88 to the rouble.

Total foreign trade expressed in billion zlotys breaks down as follows for 1984 (1983 totals in parentheses). Exports: 1,310 (1,078.2); imports: 1,161 (959.8); positive balance of exports over imports: 149 (118.4).

Translated into dollars and roubles, the foreign trade breakdown shows a dollar surplus of 1.69 billion for 1984 (1983 = 1.59 billion); and a rouble deficit of 0.6 billion (1983 = 0.5 billion).

According to the 1985 Plan, trade in Western currency will increase — exports by 1.8%, imports by 10.5%. The trade deficit in roubles will widen to 5.7 billion by the end of 1985, most of that total accruing to the Soviet Union.

Imports are scheduled to expand, both from the convertible currency area (+5%) and the rouble area (+9%). A freeze on the import of capital equipment from both areas is planned, but raw material imports will expand by some 8.4% from the convertible currency area and by some 5% from the rouble area.

Even if 1985 Plan targets are met, overall imports will still be some 20% below 1979 import levels and 35% below import levels reached in that year in trade with the West.

Implications for Trade with the West

In the longer term, Poland's economic development will be governed to a large degree by the viability of the scientific-technical cooperation agreements with the Soviet Union entered into last year. These relate principally to Polish input to the proposed new natural gas pipeline from West Siberia; cooperation in nuclear energy projects; research, development and production in the biotechnology and electronics sectors; and manufacture of automotive vehicles.

This is not to say, however, that Poland will ignore the West; for reasons outlined earlier, it cannot afford to. The reform program introduced by General Jaruzelski contains elements geared to expansion of Polish trade with the West:

- Approximately 150 state firms and 100 private enterprises have been granted official permission to trade abroad;
- Over 2,000 Polish firms are authorized to use a proportion of their foreign-currency income to underwrite imports;
- The system of auctioning hard currency is being extended;
- A new decree passed in mid-1985 allows Polish foreign trade associations to use their own cash reserves to provide investment credit to manufacturers and help underwrite export-oriented investment;
- The new joint venture program for the food processing industry presupposes import of Western knowhow and plant and makes specific financial provision for it; and
- The 1985 Plan calls for the importation of coffee, tea, citrus fruit and other foods to be paid in hard currency or via countertrade.

This year (1985), 82% of imports from the West will relate to basic industrial raw materials; 11% is earmarked for consumer goods and only 7% for capital goods. Prospects for Western exporters are best in the case of Polish firms already involved in exporting to the West.

GERMAN DEMOCRATIC REPUBLIC: According to Plan

As President of the German Democratic Republic (GDR), Erich Honecker has been the most outspoken of COMECON heads of state in his insistence that economic cooperation with the West has not proved to be such a bad thing after all - and not only for East Germany but also for COMECON as a whole. After all, trading with the West does not necessarily imply an intention to espouse Western ideology and values.

To mitigate Soviet displeasure, Honecker formally re-affirmed his country's loyalty and commitment to Moscow in September 1984, but eschewed references to West German "revanchism" (one of Soviet Foreign Minister Andrei Gromyko's favorite epithets) and quoted official Kremlin doctrine to the effect that "smaller" states (the GDR is the tenth largest industrial nation in the world) must also play a part in the quest for peace.

Mr. Honecker has one or two favorite sayings of his own, the most frequently-quoted being *Koalition der Vernunft* (coalition of reason), a phrase which conveniently covers both political and economic *détente* without implying any shift of political allegiance or alignment.

As it happens, the GDR President is in a more secure position than most of his COMECON counterparts: the country is firmly on schedule as far as the 1985 Plan is concerned; moreover, in the period 1981-84, East Germany proved to be the most resilient and most consistent performer in COMECON.

The "winds of change" identified in the Soviet Union following the advent of Mikhail Gorbachev promise to blow favorably for the GDR. Mr. Gorbachev is "impressed" and has said so: East Germany, he points out, is one COMECON country which has combined progressive economic planning and labor force commitment to develop products which are genuinely competitive in world markets. When the full details of the Soviet Union's revamped *Five-Year Plan 1986-1990* are approved by Mr. Gorbachev, it will come as no surprise if an East German matrix is readily identifiable.

Performance and Prognoses 1984-85

Official GDR Politburo figures for the period 1981 through 1984 claim year-on-year growth of net material product at 4.3%; for 1984 alone, this figure is recorded as 5.5%.

Overall, industrial production rose by 4.2% in 1984, with significant growth in lignite (+6.8%); electricity (+4.9%); natural gas (+6.6%); steel (+4%); synthetic fibers (+6.6%), lathes (+8.0%); pumps (+7.9%); paper, cellulose and printing industry equipment (+11.6%); and consumer durables (refrigerators [+7.4%], colour televisions [+19.2%], washing machines [+4.3%], furniture [+8.1%], and wristwatches [+18.8%]).

1984 was also a good year for East German agriculture. Gross production increased by some 10%, with crops (+13.8%) outpacing livestock (+8.0%). The record grain harvest of 1983 (11 million tonnes) was bettered in 1984: thanks to favorable weather, 11.5 million tonnes were harvested last year.

1984 saw a further decrease in total new investment (– 3.5%); this means that investment has fallen by

some 10% over the last three years. In some sectors, however, there was improvement: construction, for example, showed a 7.7% increase in 1984.

Foreign trade in 1984 was in surplus overall and, for the first time in a decade, there was a surplus in trade with the Soviet Union and the rouble area as a whole. A small deficit was registered in trade with the West as exports decreased and imports increased; the trade deficit with West Germany improved in 1984, less because exports increased (+0.6%) than because of a sharp fall in imports (−17.5%).

The Plan for 1985 differs little from its predecessor, with net material product slated to grow by 4.4%, gross industrial production by 3.8% and gross agricultural output by 0.8%; no growth in investment is built into the Plan.

In strategic terms, the 1985 Plan stresses recycling on the one hand and modernization/automation on the other. Modernization programs focus on electricals, electronics and micro-electronics. According to official forecasts, the "robotics" sector will grow by 18% in 1985. (East Germany already has the largest and most advanced computer industry in COMECON.)

The 1985 Plan is on schedule. Despite a hard winter, initial targets have been achieved and even surpassed. Good results are recorded for industry as a whole, construction, mining and agriculture; and "robot" production has continued apace, with an estimated 13,000 new units produced.

1986 and Beyond: Problem Areas

The next Five-Year Plan must accomodate certain broad strategies:

- How to satisfy domestic consumer demand and step up manufacturing output to meet not only home market needs but also the increasingly stringent requirements imposed by Moscow with regard to exports from COMECON to the Soviet Union;

- How to maintain and intensify export competitiveness to the point where Soviet demands are met *and* trade with the West intensified so that the GDR can be certain of access to Western technology, goods and raw materials;

- How to revamp the GDR's agricultural structure: the present arrangements (product specialization, strict separation of livestock production and crop cultivation) have proved inefficient, with coordination virtually impossible and transport/distribution problems often insurmountable; and

- How to combat progressive and economically debilitating deterioration of the environment. The industrial region of Upper Saxony is particularly hard-hit by excessively high atmospheric pollution caused principally by industrial use of lignite rather than coal or oil. Further, the southern regions of East Germany are regarded as the most polluted in all Europe in terms of sulfur dioxide (acid rain) emissions.

In addition to the expenditures implicit in developing programs to meet the above challenges, the GDR is heavily committed to military and paramilitary funding; the country has the second-best equipped military force in the Warsaw Pact (after the Soviet Union) and allocated a 6.7% increase to its military budget in 1985.

Investment: Underutilized Assets?

If longer-term economic growth is to be sustained, a reappraisal of the GDR's investment strategy is inevitable. As noted, investment has fallen by around 10% over the course of the last three years; there are two schools of thought as to why.

The first takes the straightforward view that net hard-currency indebtedness (*i.e.*, gross debt less deposits in Western banks) is being reduced to preclude any repeat of the liquidity problems which peaked in 1982. According to an OECD survey released in early 1985, total European COMECON hard-currency indebtedness (excluding the Soviet Union) at yearend 1981 was marginally in excess of US$60.3 billion, some $25 billion of which was attributed to Poland alone. East Germany's share was estimated in excess of $12 billion at yearend 1981; by yearend 1984, this figure had been reduced to somewhere around $8 billion.

The second school accepts these figures (and that a strong dollar has exaggerated progress in debt reduction), but argues that the real motivation is not prudent housekeeping but a need to improve creditworthiness (*e.g.*, by reducing the ratio of net debt to exports).

Recent developments suggest that the second interpretation has much to commend it. Certainly, in 1984, renewed confidence in the GDR's economic prospects was evident. A series of government-backed loans from West Germany re-established the GDR in Western eyes as one of the better credit risks; Swiss, Japanese, U.S. and Arab banks participated in these loans. Further, East Germany was back in favor in the Euromarkets, where it raised over US$1.1 billion last year. At the same time, East Germany's assets on deposit in the West rose to some US$4.6 billion. In short, the GDR has money to spend and a much-improved credit rating.

Conceivably, the GDR will capitalize on its improved financial position and standing with the West to act as a conduit for COMECON generally. Equally conceivably, the GDR may be on the brink of initiating a series of spectacular purchasing programs to acquire Western goods and technology.

The second possibility gained currency in June 1985 when France's Prime Minister Laurent Fabius announced after a visit to East Berlin that France and East Germany intended to increase reciprocal trade fivefold between 1986 and 1990: at present, trade between these two countries is valued at some FF 4 billion (US$450 million) annually.

Implications for Foreign Trade

For 1985 as a whole, GDR foreign trade is projected to grow by some 8%; trade with other centrally planned economies will grow by 9% and trade with non-centrally planned economies by some 6%. Imports from the West will show barely perceptible growth, and will have a total value of around US$4.5 billion (assuming no major shift in investment policies in the final quarter of the year).

The economic cooperation agreement concluded with the Soviet Union is central to East Germany's future foreign trade performance. This agreement requires the GDR to retool, expand and modernize its manufacturing base to ensure export to the Soviet Union of high-quality industrial consumer goods, manufacturing materials, and plant and equipment, in exchange for oil, gas and raw materials shipments in unspecified quantities.

The new Soviet emphasis on improved-quality imports from its COMECON satellites will inevitably make exporting to the West more difficult, since the products are precisely those which, to date, have been most readily sold in the Western marketplace.

In the final analysis, trade with the West boils down to acquisition of technology and knowhow commensurate with *Soviet* expectations. Accordingly, the key areas of opportunity promise to be the following:

- waste recovery and recycling technology
- energy conservation and recuperation plant and technology
- lignite processing
- metallurgical processing equipment and spare parts
- agricultural and specialty chemicals
- irrigation and drainage process technology
- speciality manufactured products
- glassware
- ceramics
- biotechnology; and
- knowhow and equipment specifically conducive to modernization and rationalization of industrial manufacturing techniques and product quality control (computers, robotics, micro-electronics, and microprocessors).

CZECHOSLOVAKIA: "No Development, Only a Situation"

In 1984 and the first half of 1985, significant social, economic and political initiatives in Czechoslovakia were conspicuously absent. "There *is* no development in today's Czechoslovakia", says one commentator, "only a situation".

The *régime* has many detractors, both within and without. Predictably, perhaps, specific criticisms are often distorted by rhetoric and hyperbole.

Nevertheless, they are not rejected out of hand by the government and the party élite. In an address to the National Assembly last year, Premier Lubomir Strougal conceded that:

- Productivity was too low and product quality increasingly non-competitive;
- Capital was in too short supply and investment intentions virtually non-existent;
- Industrial innovation was rare and industry was excessively energy and materials intensive (*i.e.*, smokestack rather than microchip);
- Demand for quality consumer goods, both for domestic consumption and export markets, consistently outstripped supply; and
- Quality of life was being progressively eroded, with absenteeism in industry reaching unacceptable levels, fraud and petty corruption on the increase, and alcoholism reaching chronic proportions.

Prognoses and Performances 1984-85

In 1984, net material product rose by 1.5%, gross industrial output by 3.9%, agricultural production by 3.6%, gross investment expenditures by 4.1% and real disposable incomes by 0.7%. Good results in engineering (+6.5%) and the electro-technical sector (+12.2) were offset by decreased (−10%) output of coal, coke, steel, nitrogen-based fertilizers, TV sets, motorcycles and glassware. The overall increase in gross industrial output was achieved by virtue of energy and raw materials-related expenditures that were significantly over-Budget in terms of the 1984 Plan.

Gross agricultural output increased in 1984 (+4.2% for vegetables and +3.2% for livestock); there was an exceptional - record - grain harvest of some 12 million tonnes.

Czechoslovakia's foreign trade is discussed in some detail *infra*.

The Plan for 1985 anticipates 2.3% growth in net material product, no decrease in agricultural production, no increase in gross investment, and no change in real disposable incomes. Emphasis is on the need to construct and/or modernize/refurbish existing facilities. In all, two-thirds of budgeted investment is earmarked for "productive" sectors (*i.e.*, agriculture, engineering, electronics and metallurgy). Priority growth targets within industry include engineering (targeted growth = 6%), electronics (+10%) and pharmaceuticals (+7%); by contrast, coal mining is scheduled to decrease and output in the metallurgical sector to show no change. An expansion of electricity generation is anticipated.

Irrespective of whether the 1985 Plan is met in all its indicators, overall 1981-85 Five-Year Plan goals will not now be achieved.

1986 and Beyond

The Five-Year Plan 1986-1990 will be approved and finalized at the next Party Congress in March 1986.

An average year-on-year economic growth rate of 3.5% is projected over the life on the Plan. The success rate of previous five-year plans does not inspire confidence.

The 1986-90 Plan lays stress on ensuring rapid technical/scientific progress; development programs are postulated with respect to nuclear energy, electronics, robotics, flexible production systems, energy and raw material economization, and biotechnical research and development. These programs have all been announced in the past and, to date, have proved incapable of realization in line with Five-Year Plan expectations.

Foreign Trade

In 1984, total exports increased by 10% and total imports by 10.4%. These increases arose primarily in trade between Czechoslovakia and other COMECON countries. Trade with the West showed a decidedly more modest 3.9% rise in exports and a 3.0% rise in imports.

Trade with COMECON showed a deficit in 1984 of some 560 million roubles.

Trade with the West saw a decreasing market share, particularly as regards engineering exports. To help service its debts, Czechoslovakia was obliged to substitute exports of raw materials and semi-finished products for its dwindling exports of manufactured goods. The 1984 trade surplus of US$800 million showed a $200 million decline over 1983, although it enabled Czechoslovakia to cut its indebtedness to $3 billion, the lowest relative indebtedness of any COMECON member. It is significant that exports rose considerably faster than imports in terms of volume: actual receipts dropped, however, because lower-quality goods attracted lower prices in the marketplace.

The 1985 Plan anticipates a 4.7% increase in trade with COMECON member states; concrete indicators for trade with the West were not given.

The *Program of Long-Term Economic and Scientific/Technical Cooperation* signed by Czechoslovakia and the Soviet Union runs in the first instance until the year 2000. This program stresses cooperation in engineering, chemicals, energy, metallurgy, consumer goods manufacture, agriculture and transport. Additionally, it assumes coordinated investment strategies and direct cooperation between ministries, institutions and individual enterprises in both partner countries with a view to creating "mixed" enterprises and joint ventures at production, sales and R & D levels.

Clearly, the Program will tie the Czechoslovakian economy even more closely to that of the Soviet Union; Soviet insistence on higher-quality imports from fellow COMECON states will create a further drain on Czechoslovakia's already dwindling export attractions for the West and, as a result, will cut into the hard-currency earning potential it needs in order to pay for Western goods and technology.

It remains to be seen how the Czechoslovakian Government will make good its announced intention to clear its current US$2.5 billion hard-currency debts before the end of 1985 *and* import some $2 billion in Western plant and equipment. Among the strategies under review:

- Negotiating a short-to-medium term (7-year) bank loan in the West;
- Making available additional hard-currency import funding to domestic enterprises which perform best in export markets; and
- Concluding a deal with Libya and Iran whereby oil imports from those two countries are offset by supplies of plant, machinery and technical assistance.

As far as immediate prospects for Western suppliers are concerned, the most promising approach appears to lie in exporting materials and components which are likely to contribute to a subsequent boost in Czechoslovakian exports both within and outside COMECON. Key areas include:

- automotive components and materials
- electro-engineering components and materials
- chemical and (particularly) petrochemical modernization equipment
- environmental protection plant and knowhow
- pulp and paper industry plant and equipment
- food processing plant and technology
- research hardware; and
- consumer electronics.

A limited exception to Czechoslovakia's long-standing ban on direct investment by the West is now made in the case of consumer electronics: Western firms are now being actively solicited for joint venture operations.

ROMANIA: Unorthodox Orthodoxy

The U.S. Government is one of several to have interpreted occasional flashes of independence as symptomatic of Romania's disenchantment with the Soviet alliance. Romania, one hears, is a thorn in the Soviet side. It is no coincidence that Romania enjoys U.S. most-favored-nation status.

Romania's "anti-Soviet" stance is, however, more apparent than real. Romania has been and is still one of the most authoritarian, most bureacratic and most rigidly centrally planned countries within COMECON. It also has one of the least enviable human rights records, a fact sometimes overlooked by those disposed to applaud Romania's independence in matters international.

Prognoses and Performance 1984-85

1984 saw a 7.7.% growth in net material product. Gross industrial output increased by 6.7% and agricultural output by 13.3%.

Strong growth was reported for steel (+12.5%). Growth in the metallurgical sector overall was 14.6%. Automotive production increased by an impressive 39.4% but vehicles were often sold at a loss on foreign markets. Oil production shaded by 1.2%, coal by 0.5%; by contrast, natural gas showed 2.2% growth.

Agriculture saw a record grain harvest of 23.4 million tonnes, almost half as much again as in 1983; this spectacular improvement must be seen in the context of the 1983 harvest, however, which was disastrously low. Livestock production grew imperceptibly, but non-grain crops showed 9% growth and sugar beet performed particularly well (+ 45%).

Rationing is still in force and distribution problems persist. Total state revenue grew by 5.5% and inflation was declared "non-existent".

Investment was up 6.1% in 1984. The year also saw completion of the eleven-year Danube-Black Sea Canal project. When (if) West Germany completes the final stage of the Rhine-Main-Danube Canal, there will be a direct link between the North and Black Seas.

As noted, energy supply problems persist. Stocks were depleted and energy had to be imported in an effort to maintain industrial capacity levels, notably in petrochemicals. Little progress is discernible towards the declared goals of energy conservation and energy-cost reduction via rationalization in industry. The private sector suffered, however, to the extent that blackouts and power-cuts were imposed: the use of domestic electrical appliances was forbidden during working hours, household heating was pegged at 16°C maximum and street lighting was cut back to virtually zero. Offenses under the regulations carred stiff penalties (heavy fines and/or imprisonment).

The Plan for 1985 envisages a 10% growth in net material product with industrial output up by 7.5% and agriculture by 6-7%. Investment is slated to grow by 8.3%. Assuming a zero rate for inflation (!), overall consumer demand will grow by a modest 1 to 1.5%.

The Plan seems optimistic, not least as regards the projected growth in labor productivity (+14.7%). Understandable emphasis is laid on energy production; it is accepted that steel output will decrease. Key areas of manufacture identified in the Plan include automation and ADP equipment,

instruments, optics, and hydraulic and pneumatic equipment. The 1985 Plan received a setback when it was confirmed early in the year that the 12.6 million tonne confirmed target for oil production would not be met.

Longer-Term Goals

A surfeit of optimism may also characterize the announced Plan for 1986-1990 (*see* box) inasmuch as no single annual net material product growth target was met under the 1981-85 Plan.

ROMANIA: THE PLAN FOR 1986-90

Indicator	*Annual % Growth*
Net material product	7.6 - 8.3
Gross industrial output	6.0 - 6.5
Labor productivity in industry	10
Gross agricultural production	5.4 - 5.8*
Gross investment	1.8 - 2.5
Real volume of consumption	0.6 - 0.7
Consumer prices	1.1 - 1.3
Exports (total)	8.7 - 9.3

* Five-year growth 1986-90 over 1981-85.

The 1986-90 Plan anticipates much higher growth than over the previous five years in productivity and net material product; other main indicators (capital investment, foreign trade turnover, retail sales) are lower. Renewed priority is given to energy (oil, brown coal, natural gas), mechanical engineering and chemicals, while increases in agricultural output are predicted on the basis of extensive irrigation and mechanization.

The growth in labor productivity presupposes the introduction of new technologies and modernization of existing plant and equipment on the one hand and improved management organization on the other.

As this *Overview* went to press, a new levy was proposed to help finance local investment; compulsory six-days-per-year unpaid community work was introduced for all citizens of working age; and up to 50%-of-basic-pay penalties were announced in the event of annual targets not being met. Additionally, a decree published in September 1985 introduced a system of financial incentives and disincentives for ministers, managers and technicians in the extraction industries and in export-related sectors who meet or fail to meet productivity targets.

Foreign Indebtedness

President Ceausescu declared at a press conference in Bucharest in September 1985 that Romania intends to repay all its foreign debts "within the next two to three years" and that half the country's 1980 debt will have been repaid by yearend 1985. Citing high interest rates in the West and "imperialist" financing policies, Ceausescu noted that the country's foreign indebtedness had exceeded US$10 billion in 1980; net debt is now below $5 billion (helped by a strong dollar which reduced the value or Romanian non-dollar denominated indebtedness). Although Romania requested a new international credit of $150 million in June 1985 to alleviate cash-flow problems, "no further recourse to foreign credits is planned", said Ceausescu.

Foreign Trade

Total exports increased by 16.5% in 1984; exports to the West increased by approximately the same percentage, with petrochemicals and foodstuffs forced intensively. Imports were pruned to 9.6% growth overall, although hard-currency imports grew by 13.1%. The 1984 trade surplus with the West totalled some US$2.4 billion.

The 1984-85 winter hit exports to fellow COMECON countries. The Soviet Union has refused to guarantee oil supply levels over the 1986-90 Plan and has started to charge hard currency or demand hard-currency grade goods in exchange for oil deliveries.

The scale of Romanian imports from the West over the next five years depends largely on the country's success in exporting foodstuffs and petrochemicals. Opportunities for Western firms will exist, however, to the extent that their products are compatible with the 1986-90 targets. Key areas are identified as mining and extractive industry technology and equipment, plant modernization and automation equipment, irrigation technology, and advanced agricultural machinery.

HUNGARY: Reform Reformed

In late 1984 the Hungarian state gazette *Magyar Közlöny* published in successive issues a series of new decrees and laws which, taken together, constitute a major shift in Hungary's economic policy. Close on fifty detailed regulations conspire to inject a high coefficient of entrepreneurism into the centrally planned system.

Whether or not the new measures mark a radical departure or merely continuation of the long process of economic reform first instigated back in 1968 is, ultimately, immaterial. The plain fact is that the new rules, which took effect as of January 1, 1985, offer new scope for initiative, competition and market diversification; moreover, success in the marketplace is rewarded and failure penalized. Specifics of the reform package are discussed *infra*.

The new reform package will enhance Hungary's attractions to Western companies and financial institutions. Over the last two years, Hungary's indebtedness has been reduced: significant improvement in net-debt-to-export ratio (from 247 at yearend 1981 to 185 at yearend 1984 according to OECD estimates in March 1985) has restored Hungary's creditworthiness and standing in international and Euromarkets. Additionally, Hungary's longer-term goals include relaxed rules on "mixed" (*i.e.*, joint) ventures, the establishment of duty-free zones, more favorable regulations on profit repatriation, and gradual installation of a convertible commercial-rate *forint*.

Hungary was the first COMECON country to permit the sale of bonds to enterprises and private individuals. The market has progressed since 1982 but is still tiny (±US$30 million). In March 1985, a first floating-rate bond was introduced in the form of a seven-year 9% issue carrying a premium which fluctuates with company profits. The next logical step would appear to be the issue of floating-rate bonds with no maturity, not unreminiscent of share issues in the West.

Prognoses and Performances 1984-85

In 1984, net material product grew by 2.8% overall. Gross industrial output was up 2.6%, agricultural production by 2.5%. Investment decreased by 1%. Consumer expenditure grew by 1% in real terms; consumer prices increased by 8.3%. Specifics of foreign trade are discussed *infra*.

A more detailed breakdown of these official government figures reveals that strongest manufacturing growth was registered in chemicals (+7.8%), pharmaceuticals (+ 7.4%), aluminum products, electrical machinery and appliances, telecommunications, synthetics, paper and meat processing (all +6% or more). These improvements were partly offset by decreases in coal mining, precision engineering, metal products, cement, asbestos, and poultry processing. In agriculture, crop production was up 4% and livestock production 1%.

The 1985 Plan anticipates net material product to grow by 2.3 to 2.8%, gross industrial output by 3% and agricultural production by 1%. No figure is included for investment growth. Consumer demand is projected to increase by between 1 and 1.5%, and wages will grow at the same pace as inflation, namely by 7 to 7.5%.

The Hungarian Communist Party Congress in March 1985 addressed itself to problems of stagnating standards of living, increasing corruption, the parallel ("black") economy, and residual "inequa-

lities" in Hungarian society. A solution to some, if not all of these problems seemed to lie in economic growth and continued economic reform. Accordingly, the longer-term prognoses are more ambitious.

The 1986-90 Plan

Successful implementation of the next Five-Year Plan (*see* box) depends to a large measure on how effective Hungary's reform package proves to be.

HUNGARY: THE NEXT FIVE YEARS (1986-90)

Indicator	Annual % growth projected in plan
Net material product	2.7 - 3.1
Gross industrial output	2.4 - 3.0
Gross agricultural production	1.5 - 1.8
Investment	4.4 - 4.9
Private consumption	1.6 - 1.9
Real disposable incomes	0
Exports	6.5 - 6.8
Imports	3.4 - 3.5

The key elements of the 1985 reform package are:

- Greater freedom for enterprise managements in the use of resources. Emphasis is laid on effective reaction to market forces rather than central government directives. However: industry sectors providing essential goods and services (*e.g.*, energy, transport, defense) will be controlled directly from Budapest as before. These account for between 20 and 25% of all enterprises;
- Greater freedom accorded enterprise management is matched by greatly increased management accountability. Ultimate control over business strategy is vested in the workforce which resolves on all major issues of longer-term significance and, collectively, takes on the function of employer, with the power to appoint or dismiss management, set specific business objectives, and require specific progress reports. Profitability is a primary objective: since profits are distributed to employees after fiscal and other obligations have been met, the workforce has a decisive say in how profits are earned, distributed or reinvested. Employees communicate their wishes via enterprise councils to which they elect 51% of members or, in the case of smaller entreprises (*i.e.*, with less than 500 employees), appoint management by direct vote;
- Emphasis on diversification of business activities to stimulate competition both in terms of price and quality; and
- Elaborate provision for financial incentives and disincentives (bonuses and fines) applicable to comparative efficiency and profitability. These incentives apply to management and employees alike.

It can be argued that the economic reform program is essentially a domestic matter. In Hungary, however, there has long been close interaction between domestic and foreign economic strategies and the 1985 reforms will intensify this interaction. Two specific reforms testify to Hungary's clear determination to compete on world markets:

- New pricing regulations prescribed by the National Office For Materials and Prices specifically link domestic market prices and "foreign trade" (export) prices; and
- A comprehensive new law outlawing unfair business practices is designed to "reinforce international connections" and to ensure that "a modern background of competition law underpins those Hungarian economic organizations competing in the international marketplace".

There could be no clearer statement of Hungary's commitment to step up trade outside COMECON.

Foreign Trade

Hungary's foreign trade ambitions emerge clearly from the above discussion. Much depends on the Program of Economic and Scientific Cooperation concluded with the Soviet Union which will run through the year 2000: Soviet energy and raw materials supplies must be maintained at at least 1985 levels if manufacturing capacities are to be exploited. All things being equal, trade with COMECON countries will expand by no more than 2.2 to 2.7% annually over the next five years, with exports outdistancing imports.

Hungary's trade with the West will focus on exports of pharmaceuticals, pesticides and food products and imports of plant and equipment conducive to modernization, energy conservation and recuperation and waste recycling. Hard-currency earnings will continue to benefit from a strong tourist sector. Under the reform program, reinvested profits of "decentralized" enterprises will be directed primarily towards the ADP and telecommunications sector (Hungary's largest computer manufacturer, Videoton, sells some 85% of its output to the West, and the country's leading software houses, Szamalk

and SZKI, already supply clients throughout Western Europe and Japan). Strong interest is also expressed in food processing technology, agricultural machinery and environmental protection knowhow and processes (the last in response to an articulate and expanding ecological lobby).

According to Trade Ministry sources, there will be some fifty joint ventures involving domestic and Western enterprises by yearend 1985. The fiscal obligations relating to "mixed" companies (*i.e.*, Hungarian-registered companies whose shares are partly foreign-held), foreign permanent establishments and Hungarian-source royalty income were consolidated in decrees issued on January 1, 1985, by the Ministry of Finance and the Council of Ministers.

The shifting patterns of economic thinking in Hungary will be monitored closely in the West and in Moscow, where, in Mikhail Gorbachev, Hungary detects — perhaps prematurely - a kindred spirit.

BULGARIA: A Season of Austerity

In mid-September 1985, immediately before this *Overview* went to press, the Bulgarian Government announced a package of austerity measures which attest to the critical condition of the country's economy. The twin pillars of the Bulgarian economy, industry and agriculture, are crumbling.

Bulgaria's leader, Mr. Todor Zhivkov, discounts any economic mismanagement on the part of his government and blames forces outwith his control: an exceptionally severe winter in 1984-85, followed by the worst drought Bulgaria has experienced this century.

The austerity measures are discussed in more detail *infra*. It seems scarcely feasible that they will be sufficient to secure 1985 Plan targets and meet overall Five-Year Plan goals.

Performance and Prognoses

In 1984, net material product grew by 4.6%; gross industrial output increased by 4.5% and gross agricultural production by 6.8%.

In industry, strong growth was recorded in machine building (+9.8%) and electronics/electrotechnical (+10.9), two sectors which benefitted particularly from new emphasis on intra-COMECON trade. Chemicals grew by 6%. Energy and raw materials output increased more modestly (+3.1%) and the first signs of energy supply problems were detected.

Agricultural production growth is misleadingly high to the extent that the previous year had witnessed a 7.2% decrease. Vegetable produce grew by 13.9% and livestock by 1.1%.

Investment decreased by 1.6% in 1984 to below 1982 levels. Net hard-currency indebtedness decreased from US$1.7 to $1.4 billion, in part due to statistical adjustment necessitated by a strong US dollar. Consumer expenditure increased by some 2.5%.

Foreign trade developments are reviewed under a separate heading.

The 1985 Plan anticipated net material product growth of 4.1%; industrial output was to grow by 5.2% and agricultural production by 3.2%.

Individual growth targets accorded top priority to ferrous metallurgy (+7.8%), chemicals (+26.5%), engineering (+11.6%) and lignite (+14.2%). 4.2% growth was projected for light industry as a whole, but specialized food processing was expected to grow by as much as 15%.

The 1985 Plan stressed projects conducive to waste recycling, energy conservation and recuperation and reduction of raw materials consumption.

Investment was slated to grow by between 5 and 8%, and real disposable incomes by some 3%.

The austerity package introduced in September 1985 implies that these projections are not being fulfilled.

The Council of Ministers decided that, "to compensate for losses inflicted upon the national economy by the natural calamities of 1984 and 1985", sharp price rises would apply with immediate effect to gasoline and diesel (+35%), industrial drinking water (+260%), domestic drinking water (+66%), electricity (+58% overall, with higher charges for industry than for domestic consumption), construction materials (+20-38%), and services (+13%). Prices for electrical domestic appliances

are pegged 30% higher and automobile prices by 12%.

There have also been increases in alcohol prices, imported goods, and products manufactured locally under license; these include coffee, beer, specialty delicatessen items, cigarettes and confectionery.

One can speculate that there are serious and longer-term weaknesses in the Bulgarian economy which have conveniently been veiled by the severe winter/drought in 1984 and 1985. Mr. Zhivkov himself has repeatedly criticized waste and profligacy in the deployment of agricultural and energy resources, and the Soviet Union has on several occasions singled out Bulgaria for special mention as a supplier of less-than-adequate quality goods in exchange for Soviet energy supplies.

Serious infrastructural problems persist: environmental pollution, serious throughout COMECON, is particularly acute in Bulgaria, where progressive deforestation and soil erosion is taking a heavy economic toll; energy stocks are depleted and distribution systems lax; nuclear and thermal power stations are running well below capacity; and Bulgarian industry has failed to implement a rational modernization program (costly modern equipment has often proved impossible to integrate into obsolescent production chains).

The crisis in agriculture cannot be attributed solely to adverse climatic conditions. The Bulgarian Government *allows* a limited amount of private enterprise in regard to handicrafts, retail trading and services, and apparently *welcomes* some privatization in agriculture. It is readily understood why: in 1984, 13% of arable land was privately-farmed but 25% of total agricultural produce was derived from it — sheep and poultry (38%), cattle (29%), pigs (20%), meat (40%), fruit (37%), vegetables (33%) and animal fodder (22%).

Foreign Trade

Bulgaria's foreign trade in 1984 saw exports increase by 9.7% and imports by 6.9%. The trade deficit with COMECON narrowed. Exports to developping countries increased substantially (+24%), whereas imports from the Third World grew by a mere 5%, the net result being a trade surplus of some US$1.2 billion. Trade with the West deteriorated for the fourth consecutive year: exports decreased by 8% and imports increased by 1.6%, resulting in a trade deficit of $575 million.

Dependence on trade within COMECON and with the Soviet Union is massive and increasing. Bulgarian hard-currency indebtedness is the lowest within COMECON and will be reduced even further, despite a US$100 million foray into the Euromarket in May 1985.

Prospects for Western exports to Bulgaria are not considerable; indeed, they are diminished in the light of the new austerity measures.

Some opportunities remain, however, particularly with regard to small-to-medium-sized firms in high-technology sectors. Bulgaria's computer industry is growing and the country is already the largest net exporter of electronics and the biggest manufacturer of magnetic disks within COMECON. The 1985 Plan also made specific provision for acquisition of know-how and licenses in such areas as specialty chemicals, food processing and communications, together with energy conservation and recuperation equipment and technology, waste recycling systems and environmental control systems and knowhow.

Four new joint ventures were concluded with Western companies in the course of 1984.

ALBANIA: Exit Hoxha, Enter Alia

The death of Enver Hoxha in April 1985 triggered speculation that Albania's long history of self-reliant isolationism might have drawn to a close. For over forty years Hoxha had kept the tightest conceivable rein on every aspect of the country's political, economic and social life.

Albania under Hoxha was habitually referred to as Europe's least-developed state; for Hoxha himself, it was a proud monument to Stalinist orthodoxy which he had successfully defended.

Albania's new leader, Hoxha's protégé and unopposed successor Mr. Ramiz Alia, may or may not be cast in the Hoxha mould, but he is certainly no stranger to Hoxha doctrine: he has graced the Politburo for over twenty years and has been *de facto* head of state for the past three years. Alia's first official duty as First Secretary was to preside over Hoxha's funeral; his first oficial statement came during the funeral service, when he confirmed his commitment to "Fortress Albania" and predicted little change in the country's foreign and economic policies.

Whether or not these undertakings were given out of respect or out of deep personal conviction remains to be seen. There certainly *will* be changes, however: in his last years, Hoxha had made a number of overtures to European governments (notably West Germany) to encourage both economic and political exchanges. The signs are that Alia will follow suit.

A first priority, however, will be to clarify Albania's position *vis-à-vis* its neighbors. One "old enemy" is Yugoslavia; it will be Alia's task to find a solution to the "other" Albania, the 1.7 million ethnic Albanians who comprise 80% of the population of Kosovo, an autonomous province in Serbia, without prejudicing Albanian trade access through Yugoslavia.

Performance and Prognoses

Albania is a centrally planned developing economy based on agriculture, mining and manufacturing industry. The overriding principle adhered to is that of industrial and agricultural self-sufficiency.

It would appear that Albania has made significant progress towards this goal in recent years (albeit from a low base by conventional Western industrialized nation standards):

- Self-sufficiency in food has been attained and Albania is a net exporter of fruit and vegetables. More than half the available agricultural area is irrigated, grain supplies are adequate, and there are substantial herds of sheep, goats and cattle;
— Self-sufficiency in industry is secured thanks to adequate energy resources (crude petroleum, lignite, natural gas). New oil reserves were identified in the early 1980s. Dramatic improvements in the hydroelectricity sector throughout the 1970s have continued into this decade with the recent completion of the Koman complex on the Drin River. Key manufactures include asphalt, refined petroleum, iron and steel products, refined chrome and copper, petrochemicals, plastics, nitrogenous fertilizers, superphosphates, paper, ceramics, leather, cotton and polyester knitwear, raw sugar, beverages and cigarettes and tobacco. Albania is the world's third largest producer and second largest exporter of chromium ore.

- The social infrastructure includes non-contributory social insurance, free medical treatment and compulsory free education between the ages of 7 and 15 years. The physical well-being of the population is attested by one of the highest birth rates in Europe (27.5/1,000) and relatively high life expectancy at birth (66.8 years for males, 71.4 years for females).

With the exception of demographic data above, reliable statistics on Albania are very hard to come by. Statements as to growth rates, sectoral performance and the like are an amalgam of estimate, guesstimate, extrapolation and hearsay, with some hard input from published targets in *Zëri i Popullit,* the official state gazette, and mirror statistics available from Albania's trade partners.

Accordingly, let it be said only that official growth targets for 1984 and 1985 were 8.5% and 6.2% respectively and that the former target was probably missed due to the severe 1984-85 winter which seriously disrupted energy supplies.

The official *Five-Year Plan 1986-1990* stresses further development of Albania's mineral resources, at both extractive and processing levels; parallel growth in metallurgical and heavy engineering sectors; increased output of coal, fertilizers and (petro)chemicals; and further investment in hydroelectric power, copper and chrome enrichment plants, and iron and nickel mines, together with railroad and highway construction projects.

The implications for foreign trade are discussed below.

Albania has paid a heavy price for isolationism: there is *ipso facto* a shortage of highly-skilled personnel conversant with modern manufacturing technology.

Foreign Trade

Although Albania's isolationism has been stressed throughout this *Overview,* it should be said that the country does maintain diplomatic relations with upwards of 100 countries and trade relations with 50 or so, notable exceptions being the Soviet Union and (to a lesser degree) the United States,

Among Albania's principal trading partners, mention should be made of the German Democratic Republic, Czechoslovakia, Poland, Romania, Italy, Greece, France, the People's Republic of China and, latterly, Austria, Cuba, Turkey, Sweden and the Federal Republic of Germany. (The West German involvement is significant: the West German press reports that Albanian World War II reparation claims are proposed to be settled not in cash but in terms of foreign investment and technology transfers.). Trade with each country is strictly balanced to the effect that total exports exceed total imports. This is in line with Hoxha doctrine, which accepts mutually beneficial trade links but rejects any that might place Albania in a position of indebtedness.

The above policy clearly implies heavy reliance on countertrade.

Best estimates suggest that Albania's total volume of trade amounts to between US $ 600 and $ 800 million annually; of this, some $ 80 million in 1985 will be with Greece (double 1984 levels), and some $ 120 million with Yugoslavia. Trade with China, suspended in 1978, resumed in 1983 and is currently believed to be worth some $70 to 90 million annually.

It is improbable that the pattern of trade will change in the immediate future: Albania will continue to import industrial plant and equipment and precision tools and systems in exchange for exports of chromium and chromium concentrates, pyrites, nickel, copper, tinned meat, fruit and vegetables, and tobacco; bauxite, petrochemical products and coal and electricity are also exported on a case-by-case basis subject to domestic requirements having been fulfilled.

Certain infrastructural developments might indicate that Fortress Albania is lowering the drawbridge: these include a new shipping line between Dürres and Trieste, an air transport agreement signed with Turkey, opening of the border crossing with Greece at Kavkanje (closed since the late 1940s), and completion of the Albanian portion of the rail link from Skodra to Titograd.

YUGOSLAVIA: Debt, Inflation, Unrest

Times are hard in Yugoslavia:

- Yugoslavia's Economic Program for 1985 anticipated 10% inflation for the year as a whole. By the end of the third quarter, official data released by the Finance Ministry in Belgrade confirmed that inflation had soared to some 80%, by far the highest in Europe;

- The 1985 Program promised a concerted effort to reduce the country's hard-currency indebtedness, officially acknowledged to be some US $ 20 billion. No significant net reduction was evident as of September 1, 1985, the sole change in the country's debt position being an agreement reached with foreign commercial banks in August 1985 to reschedule - subject to stringent International Monetary Fund supervision - some $ 3.5 billion of debt due to be repaid between 1985 and 1988;

- The 1985 Program stressed the need to generate employment. By September 1985, some 15% of Yugoslavia's workforce lay idle. Moreover, of the 1.25 million unemployed, approximately two-thirds were below 30 years of age;

- The 1985 Program aimed at arresting an inexorable slump in real disposable incomes. Spiralling price increases and stagnating wage levels in 1985 mean that real incomes are currently (at best) 40% below those obtaining in 1981;

-The 1985 Program relied heavily on industrial output growing by between 4.2 and 4.7% in the course of the year. By September 1985, output had grown at an annual rate of less than half that projected.

Direct consequences of the deteriorating economic position have been increased reliance on the "twilight" economy; growing social unrest (finding expression in strikes, go-slows, absenteeism and similar industrial action); and a resurgence of "nationalism" in the largely autonomous republics of Croatia, Serbia and Slovenia, not forgetting continued disaffection in Kosovo, the Yugoslavian province populated some 80% by ethnic Albanians.

Two distinct trends can be discerned.

On the one hand, the Government's critics within Yugoslavia are now querying the viability of the country's maverick stance as a "half-way house" between East and West, between central planning and private enterprise. On the other, the Government itself is seemingly taking increased refuge in short, medium and long-term projections designed to convince the population and (more importantly, perhaps) the country's international creditors that an economic turnaround is imminent.

The official projections summarized below must be seen against the realities of current performance alluded to above.

Results and Prognoses

High inflation, high unemployment, low capacity utilization, eroded living standards, chronic indebtedness and stagnant investment constitute a flimsy foundation upon which to build economic recovery. It is arguable that the Yugoslavian Government has elaborated forecasts for 1986 and beyond on the basis of results in a moderately good year (1984) and conveniently disregarded the negative indicators cited here for 1985.

[For the record, official data for 1984 saw a 2% growth in net material product, with gross industrial output up 5.6% and gross agricultural produc-

tion up 1.2%. Certain industrial sectors performed well by comparison with the stagnant years 1983 and 1982: shipbuilding was up 25.6%, chemicals 17.9%, electricity 9%, and ferrous metallurgy 8.2%; others slumped perceptibly (tobacco processing by 11.6%, construction materials by 3.6%, oil refining by 2%, natural gas by 4.4%, bauxite extraction by 4.4%, cotton textiles by 6.1%, lead extraction by 15.1%, copper by 16.6%, phosphate fertilizers by 17.5%, and commercial automotive production by 3.7%).

Short, medium and long-term forecasts are long on optimism, short on detail:

- The Plan for 1986 predicts that "the most pressing problems will be resolved by yearend";

- The Plan 1986-90 predicts "economic normalization", *i.e.*, mastery of inflation, renewed (unquantified) economic growth, and improved labor productivity ratios; and

- The Directives of Economic Development to the Year 2000 (approved in August 1985) envisage *inter alia*:
- intensification of exports (their share of gross material product to increase from 22 to 40%, with real exports growing on average by 5.1% annually);
- gross material product growing by 4.5% annually;
- annual industrial growth of 5% and annual agricultural growth of 3%;
- zero unemployment; and
- foreign debt reduced to US $ 16 billion by 1990.

Little purpose is served by analyzing these projections in detail. It is relevant to note, however, that 1985 saw imports (+7%) growing at a faster pace than exports (+2%) and that, by mid-year, drastic price increases were introduced in respect of food and energy (bread up 35%, flour 48%, meat 30%, oil 41%, electricity 20% and coal 18%). Severe drought conditions in 1985 will result in the harvest being at least 10% down on 1984.

Foreign Trade

In 1984, total exports grew by 3.6% and total imports decreased by 0.9%. The overall foreign trade deficit eased by some 18%, from US $ 2.2 billion in 1983 to $ 1.8 billion in 1984. As noted above, however, 1985 has seen imports outstripping exports.

The 1985 Plan earmarks US $ 60 million for imports. Import priorities include raw materials to boost industrial production; machinery and equipment needed for modernization of industry; and knowhow and technology in the energy sector.

Enterprises importing raw materials and items conducive to boosting industrial production are permitted to spend 100% of their total hard-currency earnings. Key sectors include pharmaceutica, sanitary and baby-foods, detergents, fertilizers, synthetic rubber and agricultural disinfectants. Other enterprises are permitted to spend 50% of their total hard-currency earnings on imports; key sectors include meat and fish products, powdered milk, vitamins, animal fodder, mineral additives, soya beans, coffee, tea, agricultural equipment spares and rubber products.

Overall, the share of trade with the West is tending to decrease. Between 1971 and 1984, COMECON trade increased from 25 to 43% of total foreign trade by volume and trade with developing countries increased from 10.5 to 17%. As a result, the share of trade with the West slipped during this period from some 65% to no more than 40% at current levels. According to figures released by the Yugoslav Economics Ministry, an average annual increase in total exports of 11.9% is projected for the period 1985-1990. The corresponding figure for imports is 9.5%. Exports to the hard-currency area are projected to expand by 14.2% annually, with imports from this area growing by 11.7%.

Progressive Liberalization

Economic reform in Yugoslavia hinges on the extent to which "privatization" is permitted. In fact, some 80% of Yugoslav agriculture is already "private" (albeit limited to 10-hectare plots, although contractual farming is increasingly tolerated) and there are an estimated 200,000 private enterprises in the manufacturing and services sectors. It is perhaps a sign of the times that a major Yugoslavian bank set up a special "private enterprise department" in January 1985.

New legislation which impacts on foreign trade has been drafted and is scheduled to come into force on January 1, 1986. This will take the form of a Foreign Exchange Law, a Foreign Relations Law, and a Law on Exchange of Goods and Services with Foreign Countries. Taken together, these enactments constitute a significant revamping of foreign trade regulations in force since 1978:

- the foreign exchange system will be more centralized;

- a four-tier import system will be set up ("free", "partly-free", "quota-limited" and "subject to import license");

- hard-currency accounts will be allocated and retained on the basis of performance; and

- provision will be made for the introduction of a convertible dinar.

Of all the moves towards a freer market, however, none is more significant than the Joint Investment Law which came into effect in November 1984 in response to criticism that previous legislation had acted as a disincentive to foreign investment. The 1984 amendement to the original 1978 Law removes certain restrictions, accords greater freedom to both Yugoslav and foreign partners in negotiating contracts, offers improved accounting certainty to the foreign investor, and simplifies approval procedures. Specifically:

- There is no longer a requirement that there be a majority Yugoslav holding;

- There is no longer a requirement limiting profit distribution abroad to predetermined levels;

- There is now provision for so-called "evidence accounts" denominated in the currency of the foreign partner and thus protected against dinar devaluation;

- There are specific provisions excluding levies on the foreign partner in respect of defense and civil defense taxes; and

- The provision allowing repayment of capital and profits in the form of goods rather than cash has now been extended to include services supplied by the joint venture.

According to the Trade Ministry in Belgrade, there are some 200 such joint ventures already in place. West Germany, with 50 separate projects, is the most important investor country, although it ranks behind the United States, Switzerland and the United Kingdom in terms of capital invested. One-third of the total foreign capital invested in Yugoslavia is of U.S. origin, spread over 30 or so individual joint venture projects.

Sources and Acknowledgements

The *1985 Overview of Centrally Planned Economies in Europe* draws extensively on official government publications in each of the jurisdictions covered. Where appropriate, these sources are cited in the main text.

In addition, valuable data and insights were gleaned from the following:

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The Conference Board (*see* inside back cover)

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